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POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

BEFORE THE
POSTAL RATE COMMISSION
WASHINGTON, D.C. 20268-0001

Docket No. R97-1

Postal Rate And Fee Changes, 1997

PRETRIAL BRIEF OF
ALLIANCE OF NONPROFIT MAILERS

David M. Levy
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, D.C. 20006-3704
(202) 736-8214

Joel T. Thomas
Suite 810
1800 K Street, N.W.
Washington, D.C. 20006
(703) 476-4646

*Counsel for Alliance of
Nonprofit Mailers*

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The Alliance of Nonprofit Mailers ("ANM") respectfully submits its pretrial brief. This brief concerns the Postal Service's proposed rates for nonprofit Standard (A) mail. ANM deals with the Postal Service's proposed rates for publications in a joint brief with other users of that rate class.

SUMMARY

The proposed rates changes for nonprofit Standard (A) mail must be rejected on two independent grounds.

(1)

The Postal Service's entire rate case suffers from an overall failure of proof. This case, the most complex in the Commission's history, is perhaps the most poorly documented. Moreover, much of the documentation was submitted months after the filing of the Postal Service's case-in-chief, a delay that has denied ANM and other interested parties an adequate opportunity to test and analyze the Postal Service's cost data. In light of the Postal Service's unexpectedly high profitability, there is simply no excuse for recommending rate increases that violate interveners' due process rights.

(2)

The limited information produced by the Postal Service reveals that the attributable cost estimates underlying the proposed rates for nonprofit Standard (A) mail—particularly non-Enhanced Carrier Route (“ECR”) mail—are almost certainly inflated. The proposed rates increases for nonprofit non-ECR mail are far larger than the increases proposed for the corresponding commercial rate category. These disparate increases cannot be explained by trends in presort condition, shape, automation, dropship entry, weight, or any other cost-causing characteristic of nonprofit mail since the last omnibus rate case. To the contrary, the increases appear to result from systemic errors in the Postal Service’s attributable cost data.

First, the labor costs attributed by the Postal Service to nonprofit mail are almost certainly inflated by the phenomenon of “automation refugees”—workers rendered surplus by automation, but remaining on the Postal Service payroll and reassigned to manual operations.

Second, ANM witness Haldi has identified several nonsensical and obviously erroneous IOCS tallies for Nonprofit Standard (A) Mail—e.g., tallies for pieces that are well above the maximum weight limit for the subclass. Eliminating these tallies from the nonprofit cost base, while necessary, does not resolve the questions they raise about the integrity of the entire IOCS. Like a handful of cockroaches on a kitchen counter, these tallies suggest that less facially obvious failures of quality control may be pervasive.

Third, a significant volume of the Standard (A) mail for which nonprofit mailers pay commercial rates appears to be reported in the RPW system as commercial mail, but reported in the IOCS system as nonprofit mail. This mismatch systematically overstates the mail processing costs attributed to nonprofit mail.

Finally, the TRACS system tends to attribute an inflated share of the costs of purchased transportation to nonprofit mail.

ARGUMENT

I. THE POSTAL SERVICE HAS FAILED TO PROVIDE THE COST DOCUMENTATION REQUIRED FOR A *PRIMA FACIE* CASE.

A. The Applicable Rules

In deciding whether to approve the Postal Service's rate request, the Commission should keep in mind three basic norms of administrative procedure. First, the proponent of changeCin this case, the Postal ServiceCbears the burden of proof. 5 U.S.C. § 556(d).¹

Second, meeting the burden of proof requires reliable, probative and substantial evidence on all material issues of fact. 5 U.S.C. § 556(d).

Third, due process entitles parties affected by a proposal to adequate notice of the evidence relied on by the proponent of change, and an adequate opportunity to respond to that evidence, including the right to Aconduct such cross-examination as may be required for a full and true disclosure of the facts.@ 5 U.S.C. § 556(d); 5 U.S.C. § 3624(b).

Enforcing these norms is especially critical in postal rate cases. The Postal Service's rate filings rest on enormous masses of statistical, econometric and computerized studies and dataCmaterial whose complexity make errors easy and comprehension by third parties difficult. See Rules of Practice and Procedure for Introducing Studies and Analyses Into Testimony, 46 Fed. Reg. 45376 (Sept. 11, 1981).

Further, the Postal Service, to an extent virtually unique among regulated monopolies in the United States, has a monopoly on the relevant data as well.

¹ The procedural requirements of the Administrative Procedure Act, 5 U.S.C. §§ 556 and 557, apply in this case. 39 U.S.C. § 3624(a).

Unlikely rate cases involving railroads, telephone companies, electric utilities, or energy pipelines, postal rate cases involve an entity that is, in many respects, the only one of its kind in the United States. Literally no other firms are available to interveners as a benchmark for most of the data submitted by the Postal Service.

Moreover, postal rate cases must be adjudicated within ten months. 39 U.S.C. §§ 3624(c)(1), 3641. ANM and ALA are unaware of any other regulated industry in which rate cases of such complexity must be tried and resolved on the merits in so short a period.

To protect parties' due process rights in these circumstances, the Commission has crafted detailed rules for documentation of Postal Service rate requests. In particular:

(1) When filing a rate request, the Postal Service must simultaneously file all of the proposed direct evidence upon which it proposes to rely to satisfy the statutory ratemaking criteria. Rule 53. This evidence must take the form of either written testimony or documentary exhibits. *Id.*

(2) The supporting testimony and exhibits must be sufficient fully to inform the parties of the nature, scope, significance and impact of the proposed rate changes, and to show that [they] are in the public interest and in accordance with Title 39. Rule 54(a). To enforce this general standard, Rules 54(b) through (r) require the Postal Service to include an array of specific information in a rate request unless the Service shows with particularity in its request why furnishing such information would be unduly burdensome. Rule 54(a)(2). The required data include information on rates and standards; mail characteristics; physical attributes of mail; specialized service arrangements; total functionalized accrued costs; costs of prior fiscal years; separation, attribution and assignment of costs to individual classes and types of mail; criteria for design of the rate schedule; revenue and

volume data; financial statements and related information; billing determinants; continuing and phasing appropriations; and relevant performance goals. Rule 54(b).

(3) Additional supporting detail must be provided for studies and analysesCwhether offered by the Postal Service or any other partyCincluding statistical studies and computer analyses. Rule 31(k).

(4) The Postal Service must provide a clear roadmap for other parties to the material supporting the rate request. Each category of information specified by Rule 54(b) through (n) must be supported by workpapers sufficient Ato permit independent analysis of each cost component and an independent attribution or assignment of costs to classes and subclasses and the assignment of nonattributed or nonassigned costs to classes and subclasses.@ Rule 54(o)(2)(i). Workpapers must be Alegible,@ and must include Acitations sufficient to enable a reviewer to trace any number used but not derived in the associated testimony back to published documents or, if not obtained from published documents, to primary data sources.@ Rule 54(o)(3),(4) (emphasis added). Citations shall be Asufficiently detailed@ to enable a reviewer to identify and locate the Aspecific data used, e.g., by reference to document, page, line, column, etc.@ Id.

(5) The Commission has also adopted rules to prevent the Postal Service from burying key data under boxcars of irrelevant material. Where Arelevant and material matter offered in evidence is embraced in a document containing other matter not material or relevant,@ the participant offering the matter into evidence Ashall plainly designate the matter offered excluding the immaterial or irrelevant parts.@ Rule 31(b).

(6) Information supporting the Postal Service's case-in-chief may not be admitted into evidence unless sworn to or affirmed by a sponsoring witness.

Rule 31(a). Designation of material as a library reference does not obviate this requirement. Rule 31(b); Presiding Officer's Ruling No. R97-1/20 (Sept. 17, 1997).

(7) Noncompliance with these rules entitles the Commission to reject the Postal Service's rate request or stay the proceeding until satisfactory compliance is achieved. Rules 54(s) and 56.

B. The Postal Service's Noncompliance With The Commission's Rules

The instant docket marks a watershed in the inadequacy of the Postal Service's supporting documentation for a rate request. By general consensus, this is the largest and most complex postal rate case ever, with over 40 witnesses and a myriad of novel costing methods offered in the Service's case-in-chief. If there were ever a case where due process mandated strict compliance with the Commission's rules for documentation of rate requests, this is it. In fact, the incompleteness and opacity of the Postal Service's supporting documentation may be worse than ever.

The Postal Service's litigation tactic of burying critical data and studies in unsponsored library references has received much attention. But this shortcoming is only one of several pervasive problems. These include: (1) failure to file all of the evidence supporting the Postal Service's request simultaneously with the request; (2) failure to make key showings required by Rules 31 and 54; (3) failure to provide workpapers in compliance with Rule 54(o); and (4) failure to distinguish between the relevant supporting data and the masses of irrelevant data produced; as well as (5) reliance on unsponsored data and studies. We discuss each deficiency in turn.

Failure to file all supporting evidence with request. The purpose for requiring the Postal Service to file all the proposed direct evidence upon which it proposes to rely simultaneously with the Service's rate request (Rule 53) is obvious. Supplementing or revising the Postal Service's case-in-chief after the commencement of the ten month statutory period presents other parties with a moving target, impinging on their already limited window of opportunity to analyze the Postal Service's case and prepare their own testimony.

The Postal Service has flouted this rule continually throughout this case. Errata have followed massive errata. Supplemental testimony has materialized on the eve of hearings, and even during the hearings themselves. See, e.g., Tr. 3423 (USPS witness Nieto). Moreover, on October 14, a week after cross-examination of Postal Service witnesses began, the Service notified other parties that 50 library references many of which individually run to hundreds of pages of spreadsheets or other data in small type are now being sponsored into evidence as part of the Service's case in chief. USPS Response to Presiding Officer's Ruling No. R97-1/42 (filed Oct. 14, 1997). Supplementation of the Postal Service's case-in-chief threatens to continue: the Service has suggested that it may offer witnesses for yet additional library references that might be identified subsequently during hearings or otherwise. @ Id. at 3.

A minimum amount of errors and supplementary filings are almost inevitable in a big case. But there comes a point at which the continual stream of errata and supplemental designations of evidence, coupled with a tight statutory deadline in a case of this magnitude and complexity, work real prejudice on other parties. That point has long since been reached.

Failure to submit supporting data required by Rules 31 and 54. As noted above, Rule 31(k) establishes specific requirements for Aall studies and analyses offered in evidence in hearing proceedings or relied upon as support for other evidence.@ Rule 31(k)(1) provides that all studies and analysis other than those described in paragraph (k)(2) and (k)(3) must include Aa clear statement of Aall relevant assumptions,@ as well as Aa clear statement of the facts and judgments upon which conclusions are based, together with an indication of alternative courses of action considered.@ None of the library references reviewed by ANM and ALA include a clear statement of the facts or judgements upon which conclusions are based. Not one of them appears in any way to consider any alternative course of action other than the one reported.²

Moreover, none of the statistical studies reviewed by ANM and ALA include any description of the assumptions made, much less a comprehensive one. The formulas used for statistical estimates, test statistics, a description of statistical tests and all related computations, and summary descriptions of input data are also missing from the statistical studies or analysis reviewed by the Alliance.

Failure to provide workpapers required by Rule 54(o). Equally serious is the Postal Service's noncompliance with the Commission's workpaper requirement. The Postal Service's statement of compliance with Rule 54(o) dismisses the workpaper requirement in two sentences: AThis rule requires seven sets of workpapers to be filed with the Request. The required workpapers are supplied with the testimonies of the Postal Service's witnesses.@ Equating Aworkpapers@

² See, e.g., LR-H-60, LR-H-61, LR-H-62, LR-H-77, LR-H-78, LR-H-105, LR-H-106, LR-H-113, LR-H-130, LR-H-134, and LR-H-195.

with Atestimonies,³ and filing seven or more copies of the latter with the Commission, does not begin to satisfy Rule 54(o).

Workpapers, in the lexicon of Rule 54, are defined as much by their ends as their means. Workpapers must be legible; they must identify and locate the specific data used. I.e., A by reference to document, page, line, column, etc.; and they must enable a reviewer to Atrace any number used but not derived in the associated testimony back to published documents or, if not obtained from published documents, to primary data sources. Rule 54(o)(3), (4) (emphasis added). If the Postal Service fails to provide a clear, specific, step-by-step roadmap from a numerical result back to its ultimate source in published documents or primary data, the Postal Service has not provided valid workpapers under Rule 54.

Many of the numerical values appearing in the Postal Service's testimony and exhibits are unsupported by any workpapers at all. Key data are provided without any indication whatsoever of their provenance. In other instances, the trail of documentation vanishes into thin air only one or two steps back from the end results.³

Citations to source documents are often maddeningly vague. The reader is repeatedly steered to library references containing of hundreds of pages of spreadsheets or computer printouts, with no hint offered as to the page, column or

³ See, e.g., LR-H-77, which sets forth mail processing piggyback figures relied upon by USPS witnesses Hatfield and Daniels. LR-H-77 is virtually devoid of any citation to the source of any numbers or data included in it. Moreover, the references to it by witnesses Hatfield and Daniels invariably cite the document as a whole, not a specific section, page, line or column. See USPS-T-16 (Hatfield) at 15; USPS-T-26 (Hatfield) at 31 & App. I, pp. 6, 10, 37.

line.⁴ In other instances, the derived value appears nowhere in the library reference, but must be derived by arithmetic manipulations from two or more numbers in the library reference. In other instances, the citations are simply incorrect.⁵

Many of the workpapers are incomplete. In many instances, the electronic versions of the library references filed with the Commission lack critical information appearing only in the hard copies. The absence of any warning that the workpapers are incomplete has caused ANM and other participants to waste

⁴ LR-H-134, for example, makes continual reference to other Library References without identifying the section or page, much less the line or column from which the data come. See LR-H-134 at § 1, pp. 6, 9, 11, 12, 13, 23-28; *id.*, § 2, pp. 7, 10, 12, 13, and 43, etc.

⁵ USPS witness Crum's response to NDMS/USPS-T28-11 illustrates all of these problems. As the source for certain costs in LR-H-108, the Postal Service's "workpaper" provided only an unpaginated citation to "LR-H-106," a 49-page document. Asked for precise citations to the page, row and columns in LR-H-106 where the data appeared, the Postal Service conceded that (1) the figures cited in LR-H-108 did not in fact appear in LR-H-106; (2) replicating the figures in LR-H-108 required arithmetic manipulation of data from multiple locations in LR-H-106; and (3) the figures in LR-H-108 were incorrect. 5 Tr. 2223-24.

The documentation underlying USPS witness Wade's analysis of vehicle service drivers provides another example. The documentation included spreadsheets for 50 facilities. The Postal Service's workpapers did not include a printout of the formulas embedded in the spreadsheets. Time consuming analysis of the spreadsheets revealed numerous differences in the algorithms from one spreadsheet to the next, and numerous errors. The Postal Service did not file a new library reference (LR-H-261) correcting the errors until the last day of the discovery period.

Similar problems beset the documentation of TRACS. The library reference originally produced by the Postal Service (LR-H-84) contained a working electronic file for only the first quarter of Base Year 1996; the files for the following three quarters were corrupted and could not run. The Postal Service did not submit corrected files for the latter quarters until October 1st (LR-H-288).

hours trying to parse them. In other instances, it is the hard copies which are incomplete.

Many of the electronic spreadsheets filed as library references contain electronic links to other spreadsheets or data sources that have been filed (if at all) only as separate library references. Unless the missing linkages are loaded in the user's computer (and assigned the directory and file names sought by the linking program), the spreadsheets cannot run properly.

Many of the library references (including spreadsheets supporting the volume testimony of witnesses Tolley, Thress and Musgrave) are programmed in mainframe languages such as SAS and SORITEC, and cannot be read on a PC. Other library references are written in decades-old computer languages such as COBOL and FORTRAN. As a practical matter, these workpapers are not Alegible@ within the meaning of Rule 54(o)(3).⁶

Boxcar data production. The Postal Service has further aggravated the problem by burying the relevant supporting material under a mountain of irrelevant data. To date, the Postal Service has filed nearly 300 library references, many of which individually contain hundreds of pages or millions of bytes of data. It now appears that USPS never had any intention of relying on vast majority of the

⁶ The programs underlying USPS witness Degen's analysis of Cost Segment 3, set forth in Library Reference LR-H-218, are a good example. As the Commission is aware, Mr. Degen's methodology marks a radical departure from the Postal Service's prior method of distributing these costs. His analysis, however, was run on an IBM mainframe version of the SAS statistical program. The overwhelming majority of the SAS user community has migrated to the PC platform, and Mr. Degen's SAS programs could not be run on the PC version of SAS without time-consuming manual reprogramming. Two solid days of questioning of Mr. Degen's staff were required simply to replicate his results.

library references. Many of them are cited nowhere in the Postal Service's testimony; and the Service has proposed to sponsor only about 50, or 15 percent, of them. Of the first 100 library references, the Postal Service has seen fit to sponsor only one. USPS Response to Presiding Officer's Ruling No. R97-1/42 (Oct. 14, 1997).

Reliance on unsponsored data and studies. As several participants have noted, much of the Postal Service's case rests on data and inputs from library references that no Postal Service witness has yet offered to sponsor under oath. See, e.g., OCA Response to Notice of Inquiry No. 1 (Oct. 3, 1997) at Attachment A. These unsponsored data are not evidence, and may not be relied upon in support of the Postal Service's case. Rule 31(b); accord, Reply Brief of the USPS in Docket No. MC96-1 (March 4, 1996) at 17-19 & n. 8 (arguing that Commission may not consider OCA cost analysis based on unsponsored OCA library reference).

The Postal Service's failure to offer witnesses to sponsor these data under oath cannot be excused on the theory that they are information that an expert could reasonably rely upon as the basis for an opinion. The Commission has rejected this approach and properly so. See MC93-1 Op. & Rec. Decis. ¶ 211 (lack of a sponsoring witness made it inappropriate to admit the follow-up survey results into the record to establish the truth of matters that the survey questions themselves address, such as quantification of USPS volume).

The unsponsored data are not collateral or cumulative support for an expert's opinion: they are used, directly or indirectly, as inputs to Postal Service cost studies, and thus are being offered for their truth. Moreover, the Commission's elaborate requirements for documentation of the Postal Service's

supporting data and the errors in those data chronically unearthed in rate cases flatly belie the notion that any competent expert would reasonably rely on Postal Service data without careful independent scrutiny.

Reliance on the business record rule is likewise misplaced. The data and studies underlying Postal Service rate requests do not, by and large, have an independent business role that gives the Postal Service a stake in their accuracy. The data are, with few exceptions, created for use in litigation.

If the Postal Service's logic were accepted, the Postal Service's direct testimony could be a single sentence by a single witness: AI find, based on the Postal Service's underlying studies and data prepared specifically to prove this point, that its cost estimates and rate proposals are reasonable. The rest of the case could be unsworn library references. There would be no point to rate cases or the Commission itself. The requirement that parties offer witnesses to sponsor testimony and exhibits is a hollow one if parties can bootstrap critical data and studies into evidence by offering witnesses who attest to the conclusions drawn from the data and studies, but not to their underlying inputs, assumptions and methodology. A meaningful opportunity for cross-examination must include the latter as well as the former.⁷

The Postal Service, apparently recognizing the problematic nature of its unsponsored library references, belatedly offered to sponsor about 15 percent of them. USPS Response to Presiding Officer's Ruling No. R97-1/42. This response is too little and too late. The majority of library references remain unsponsored. Even in sponsored library references, much of the information relies on inputs

⁷ See *Mail Order Ass'n of America v. USPS*, 2 F.3d 408, 429 (D.C. Cir. 1993); *Newsweek, inc. v. USPS*, 663 F.2d 1186 (2d Cir. 1971), *aff'd*, *Nat'l Ass'n of Greeting Card Publishers v. USPS*, 462 U.S. 810 (1983).

from other unsponsored studies or compilations that remain unsponsored.⁸ Like the 500 hats of Bartholomew Cubbins, each layer of unsponsored data rests on still others.

Moreover, the Postal Service's sponsorship announcements have come far too late to allow meaningful cross-examination. The newly-sponsored library references are comparable in length and complexity to the case-in-chief of a good sized rate case only a few years ago. Meaningful scrutiny of this dizzying array of material would take several months. If these items had been filed and identified as witness-sponsored exhibits when USPS filed its case-in-chief, as USPS should have done, parties would in fact have received the necessary time. Requiring parties to assimilate this morass of materialCwithout further discoveryCin the week left before October 23, when sponsoring witnesses are scheduled to take the stand, is a caricature of due process.

The Commission's actions to enforce compliance with its own rules, and allow greater scrutiny of the Postal Service's case-in-chief, have not provided interveners with a legally adequate opportunity to scrutinize and respond to the Postal Service's cost evidence. Enforcement of the Commission's rules appears to have taken a back seat to the Commission's reluctance to invoke its authority to

⁸ For example, LR-H-106 at pages II-8, III-6, IV-6, V-1, V-2, VI-3, VI-4, VI-5, VI-6 and VI-7 relies upon LR-H-126. LR-H-77 at pages II-8B [203], II-9 [204] and II-16 [211] relies upon LR-H-127. LR-H-77 is in turn widely relied upon by other Library References, e.g., LR-H-134 relies upon LR-H-77 at many points including Sec. 8, p.35, Sec.9, p. 10, Sec. 9, p. 35, Sec. 11, p. 10, and Sec. 11, p. n10.

extend the deadline for a recommended decision.⁹ This truncated opportunity to scrutinize the Postal Service's case, however, has not produced a record that can lawfully support approval of the proposed rate changes.

C. Rejection of the Postal Services' Rate Request Is An Appropriate And Practical Remedy.

The Postal Service's noncompliance with the Commission's rules requires rejection of the Service's proposed rate changes. The Commission is at a crossroads. There will never be a more propitious time to enforce compliance with the Commission's rules. Inflation is low; the Postal Service is far more prosperous than anticipated when this rate case was filed; and no one can seriously contend that rejection of the rate requests, and requiring the Service to refile its case with proper documentation, will jeopardize the Service's financial survival. See Notice Of Inquiry No. 5 On Recognizing Interim Year Results (Jan. 28, 1998) (noting unexpectedly high profitability of the Postal Service during 1997).

⁹ For example, when ANM filed discovery requests for workpapers and other documentation underlying the Postal Service's case, material that the Commission's rules require the Postal Service to submit with its case-in-chief, the Commission declined to compel the Postal Service to respond, limiting ANM to an off-the-record technical conference on the eve of hearings.

II. THE LIMITED DOCUMENTATION PRODUCED BY THE POSTAL SERVICE REVEALS THAT IT HAS GROSSLY OVERESTIMATED THE ATTRIBUTABLE COSTS OF STANDARD (A) NONPROFIT MAIL.

A. The Disproportionate Rate Increases Proposed For Nonprofit Regular Mail Cannot Be Explained By Any Reported Changes In Its Cost-Causing Characteristics.

In this docket, the Postal Service has proposed rates for Nonprofit Standard Mail (A) Regular (Bulk Nonprofit ("BNP") Other) mail that increase sharply, while proposing only a small overall increase in rates for the corresponding commercial rate subclass (Standard Mail (A) Regular, former Bulk Regular Rate ("BRR") Other). The *letter* rates proposed by the Postal Service for Standard Mail (A) Regular illustrate the deviation between nonprofit and commercial rates in this docket. As can be seen from Table 1, letter rates within the Presort Category exhibit the sharpest contrast; Nonprofit Standard Mail (A) Regular letters *up 19 percent*, Standard Mail (A) Regular letters *down slightly*. On a percentage basis, the changes in rates proposed for Automation letters, a fairly homogeneous category, also deviate significantly (except for carrier route automation letters). ANM-T-1 (Haldi) at 5-6.¹⁰

¹⁰ At the same time, the Postal Service proposes downward revisions for Nonprofit ECR rates, while rates proposed for the commercial rate ECR subclass increase modestly. ANM-T-1 (Haldi) at 5 n. 1.

Table 1						
Standard Mail (A) Regular Postal Service Proposed Letter Rates						
	NONPROFIT RATE			COMMERCIAL RATE		
	Old Step 6	New Step 6	Percent Change	Existing	Proposed	Percent Change
PRESORT CATEGORY						
Basic Presort Letter	13.8	16.5	19.57%	25.6	24.7	-3.52%
3/5 Presort Letter	12.0	14.3	19.17%	20.9	20.9	0.00%
AUTOMATION CATEGORY						
Basic Auto Letter	10.5	12.4	18.10%	18.3	18.9	3.28%
3-digit Auto Letter	10.1	11.2	10.89%	17.5	17.6	0.57%
5-digit Auto Letter	8.8	9.5	7.95%	15.5	16.0	3.23%
Cr Rte Auto Letter	8.5	9.2	8.24%	14.6	15.7	7.53%

These disproportionate rate increases are driven by disproportionate increases in the costs attributed by the Postal Service to nonprofit mail. Table 2, taken from Dr. Haldi's testimony, compares average unit costs for Standard Mail (A) and Nonprofit Standard Mail (A) Regular (formerly third-class bulk) since 1992. ANM-T-1 (Haldi) at 7-9. The most telling comparisons are between columns 1 and 2, for FY95 and FY96. From FY95 to FY96, the unit cost for Bulk Regular Rate (BRR), "other" (the predecessor to Standard Mail (A) Regular) declined modestly, by 0.1 cent. At the same time, from FY95 to FY96 the unit cost for Bulk Nonprofit (BNP) "other" (the predecessor to Nonprofit Standard Mail (A) Regular) increased by an abnormally large amount, 0.8 cent. Considered together, these two changes narrowed the difference in unit cost between BRR "other" and BNP "other" by 0.9 cents. *Id.*

FY96 was unusual in the following respect. From FY92 through FY95, whenever the average unit cost for BRR "other" increased or decreased, the unit cost

of BNP “other” also increased or decreased, whereas in FY96 the unit cost for BRR “other” decreased slightly while BNP “other” skyrocketed upward. *Id.* at 7-8.

The unusually large increase in unit costs in FY96 carries through to Base Year 1996, which is then rolled forward to Test Year 1998. That is, the relationship between Nonprofit Standard Mail (A) Regular and Standard Mail (A) Regular rates is preserved more or less unaltered by the transformations that take place in the Postal Service models. *Id.* at 8-9.

Table 2

Third Class/Standard Mail (A)
Average Unit Cost
(cents)

Fiscal Year	BRR <u>Other</u> (1)	BNP <u>Other</u> (2)	BRR Carrier <u>Route</u> (3)	BNP Carrier <u>Route</u> (4)
1992	15.3	10.8	6.9	5.0
1993	14.6	10.4	6.1	4.9
1994	14.2	10.2	6.1	4.5
1995	14.7	10.4	6.4	4.4
1996	14.6	11.2	6.4	4.8

These disproportionate increases in unit attributable costs cannot be explained by relative year-to-year changes in the cost-causing attributes of nonprofit and commercial Standard Mail (A)—including presort condition, shape, automation, dropship entry, and weight—during the same period. ANM-T-1 (Haldi) at 10-20. Both subclasses are handled in the same manner, and mail processing cost models assume the same productivity (or lack thereof) for both. *Id.* at 20.

As the proponent of increases in nonprofit postal rates, the Service bears the burden of proving that these disparate increases in attributable costs for nonprofit mail

have really occurred. Failure to do so requires rejection of the Postal Service's rate request, at least with respect to nonprofit rates. 39 U.S.C. § 3624(a) (incorporating 5 U.S.C. § 556(d)); 39 U.S.C. §§ 3622(b)(3), 3626(a)(3). In fact, the record contains substantial evidence identifying several specific reasons why the Postal Service's attributable cost data for nonprofit mail are inflated. We now describe these factors in turn.

B. The Automation Refugee Problem Has Inflated The Mail Processing Costs Attributed to Nonprofit Standard (A) Regular Mail.

Much of the apparent increase in Nonprofit Standard (A) attributable costs appears to be the byproduct an influx of "automation refugees"—workers who remain on the Postal Service payroll despite having been rendered surplus by automation of other mail processing operations—into manual mail sorting operations. While these surplus workers appear on IOCS tallies for nonprofit mail, their costs are not attributable to the subclass, for a firm operating under "honest, efficient, and economical management" (39 U.S.C. § 3621) would not process nonprofit mail with more workers than needed to handle it.

How significant is the automation refugee problem? Between Fiscal Years 1995 and 1996, the total costs attributable to Nonprofit Standard (A) Mail Regular increased by 8.7 percent, while volume increased by only 0.8 percent. The average increase in unit attributable cost was 0.81 cents, or 7.8 percent, reflecting the small increase in volume and the large increase in total attributable cost. ANM-T-1 (Haldi) at 21. Two cost segments—clerks and mailhandlers and purchased transportation—and related piggybacks accounted for three-fourths of this increase. And clerks and mailhandlers (and associated piggyback costs) in turn accounted for three-fourths of this fraction. ANM-T-1 (Haldi) at 21.

Nonprofit mailers barcode and drop ship a lower percentage of their mail than do regular rate mailers, and thus a larger portion of nonprofit mail must be handled manually. In other words, a lower percentage of Nonprofit Standard Mail (A) Regular qualifies for worksharing discounts, which means that less of it bypasses the Postal Service network. ANM-T-1 (Haldi) at 11-19.

The increase in unit cost for Nonprofit Standard Mail (A) Regular is consistent with hypotheses that (1) the Postal Service has “automation refugees,” and (2) productivity has declined and continues to decline in areas where mail is not handled by automation or mechanization. That is, the Postal Service has an excess of displaced clerks and mailhandlers who are kept busy (at reduced productivity rates) processing mail that is not automated and does not (or can not) take advantage of drop-shipment to bypass the Postal network. ANM-T-1 (Haldi) at 22-23; TW-T-1 (Stralberg).

In this environment, the design of the IOCS tends to produce nonsensical results. For example, mail that is handled manually, at constant productivity, will have an increasing proportion of direct handling tallies. In turn, the higher ratio of direct tallies will cause an increase in the share of “not handling” tallies and costs assigned to manually sorted mail.¹¹ In other words, without any cost-driving change in manually sorted mail, total costs (and unit costs) may nevertheless be deemed to have increased. TW-T-1 (Stralberg); ANM-T-1 (Haldi) at 23-24.

The existence of an automation refugee problem also helps explain the sharp increase in mail processing costs *relative to direct carrier costs*. ANM-T-1 (Haldi) at 23; TW-T-1 (Stralberg).

¹¹ As automation has progressed, the share of “not handling” tallies has increased substantially, with a corresponding decline in the share of direct tallies. ANM-T-1 (Haldi) at 23 n. 9.

Finally, rates for the Basic and 3/5-Digit presort categories show the greatest rate increase, along with the Automation Basic category. These categories require the greatest amount of handling. The higher-than-average rate increases reflect higher-than-average cost increases, which reflect productivity changes below average (*i.e.*, a decline in productivity). *Id.*

C. Nonsensical IOCS Tallies Inflate The Reported Attributable Costs Of Nonprofit Standard (A) Mail And Betray A Pervasive Quality Control Problem With The IOCS.

Mail processing costs for each subclass reflect the IOCS tallies of clerks and mailhandlers recorded for that subclass. Unfortunately, scrutiny of the FY96 IOCS tallies for Nonprofit Standard Mail (A) Regular reveals a number of tallies that are nonsensical on their face.

In FY96, 2,568, IOCS tallies were recorded for Nonprofit Standard Mail (A). Of this total, 2,393 tallies were for Nonprofit Standard Mail (A) Regular, and 175 were for Nonprofit Standard Mail (A) ECR. Direct mail processing accounted for most of the tallies (2,533 out of 2,568). 2,362 of the 2,533 direct mail processing tallies were for Nonprofit Standard Mail (A) Regular. ANM-T-1 (Haldi) at 26-27.

Table 3 shows the recorded weight for each of the 2,362 Nonprofit Standard Mail (A) Regular tallies (*id.* at 32):

Table 3
Nonprofit Standard Mail (A) Regular
Distribution of Mail Processing Tallies
By Item and Weight

	Single Piece Tallies	Item Tallies	Container Tallies
No Weight recorded	0	29	0
Up to 1 oz.	940	533	12
1 up to 2 oz.	282	141	5
2 up to 3 oz.	115	65	1
3 up to 4 oz.	106	22	2
4 up to 5 oz.	0	0	0
5 up to 6 oz.	37	19	0
6 up to 7 oz.	9	2	0
7 up to 8 oz.	0	0	0
8 up to 9 oz.	9	5	0
9 up to 10 oz.	0	0	0
10 up to 11 oz.	11	2	0
11 up to 12 oz.	0	0	0
12 up to 13 oz.	4	0	0
13 up to 14 oz.	0	0	0
14 up to 15 oz.	0	1	1
15 up to 16 oz.	1	1	0
2.5 up to 3.0 lbs.	1 IPP	0	0
3.0 up to 3.5 lbs.	0	1 letter	0
4.0 up to 4.5 lbs.	0	1 flat	0
4.5 up to 5.0 lbs.	1 IPP	1 flat	0
6.0 up to 7.0 lbs.	1 flat	0	0
over 15 lbs.	0	1 parcel	0
Total	1,517	824	21

Seven of the tallies record a weight in excess of 16 ounces, the weight limit for Standard Mail (A). *Id.* Clearly, something is wrong with these 7 tallies.¹² Either

¹² These tallies cannot be explained on the theory that the a container or item have been measured. In all instances where weight is recorded, it is supposed to be for a single piece of mail. ANM-T-1 (Haldi) at 29-30.

the weight is in error, or the tally has been misrecorded as Nonprofit Standard Mail (A). In response to a hypothetical question about a piece of Standard Mail (A) whose weight exceeded 16 ounces, USPS witness Degen stated that:

The F-45 handbook (LR-H-49) contains no specific instructions for the disposition of such a tally. Mail class is recorded in question 23b. The question 23b instructions indicate that the Third-Class/Standard Mail (A) categories apply to mailpieces weighing less than 16 ounces. Weight is recorded in question 23g. The instruction to question 23g (LR-H-49, p. 131) are simply to record the weight in pounds and ounces, rounded to the nearest ounce, for mailpieces weighing more than 4 ounces. *It cannot be determined from the hypothetical whether the mail class was misidentified or the weight was incorrectly entered.* (Emphasis added)¹³

In addition to the tallies that recorded weight in excess of 16 ounces, another 35 tallies recorded weight between half a pound and 16 ounces. ANM-T-1 (Haldi) at 32. To have so many heavyweight tallies in a subclass with an average weight of only 1.1 ounces (ANM-T-1 (Haldi) at 20 (Table 7)) is unusual, especially the three letter-shaped tallies, one of which was reported to weigh between 15 and 16 ounces.

All tallies above 16 ounces are clearly in error, and should be disregarded when computing the cost of Nonprofit Standard Mail (A) Regular. This correction does not end the matter, however. The ability of these facially nonsensical tallies to survive the editing process suggests a far broader and deeper breakdown in the IOCS quality controls. The errors identified here are likely to be only the tip of the iceberg. ANM-T-1 (Haldi) at 31.

¹³ ANM-T-1 (Haldi) at 30-31 (quoting written response of USPS witness Degen to oral questions of ANM (filed October 28, 1997)).

D. The Reported Cost Data For Nonprofit Mail Are Inflated With IOCS Tallies For Commercial Standard (A) Mail Entered by Nonprofit Mailers.

The attributable costs of nonprofit Standard (A) mail have been further inflated by a mismatch of the IOCS and RPW data for Standard (A) mail bearing nonprofit indicia but paying commercial rates. There are several reasons why nonprofit mailers pay commercial rates for Standard (A) mail:

- (1) the Postal Service collects a revenue deficiency assessment after entry of the mail, on the ground that the mail was ineligible for nonprofit rates;
- (2) the Postal Service rejects the mail for nonprofit rates at the entry point, on the ground that the mail is ineligible for nonprofit rates; or
- (3) the mailer determines in advance that the Postal Service will reject the mail for entry at nonprofit rates.

ANM-T-1 (Haldi) at 37-45. New eligibility restrictions for nonprofit mail taking effect shortly before and during the test year have caused nonprofit mailers to pay commercial Standard (A) rates for substantial volumes of mail bearing nonprofit indicia. *Id.* at 40-43; Exh. ANM-T-1 (revised 2/9/98).

This phenomenon has created a serious mismatch between the RPW volume data and the IOCS cost data for the nonprofit subclass during the test year. Mail volumes entered by nonprofit mailers at commercial rates, and volumes subject to back postage assessments that lead to the filing of a new Form 3602, are recorded in the RPW as commercial mail. *Id.* When such pieces bear nonprofit rather than commercial indicia (e.g., meter markings or precancelled stamps), however, the IOCS attributes their mail processing costs to the nonprofit subclass. *When entry data (Form 3602s) and envelope markings do not coincide, the IOCS will attribute costs*

to one subclass, while the volumes and revenues will be recorded in another subclass.¹⁴ The subclass that is credited with extra volumes but no extra costs (tallies) will have *an understated unit cost*, while the subclass that is assigned the extra cost (tallies) but gets no credit for the corresponding volume will have *an inflated unit cost*. *Id.* at 35.

The initial cost and volume data are primary inputs to many other modeling efforts, including the roll-forward model. When these fundamental data become unsynchronized, the entire costing edifice built on the IOCS becomes unsound. *Id.* at 40.

To investigate the extent to which the sharp increase in Nonprofit Standard Mail (A) Regular unit costs may have resulted from revenue and cost data being “out of sync,” the Alliance of Nonprofit Mailers has undertaken a survey of nonprofit organizations. A summary of the results of that survey follow. Additional details are contained in Exhibit 1 ANM-T-1 (revised 2-9-98). Of 108 responses received:

- 31 organizations entered mail at commercial rates and used commercial rate indicia.
- 49 organizations entered mail at commercial rates, but used nonprofit evidencing of postage.
- 28 organizations entered nonprofit mail at nonprofit rates and with nonprofit markings, but later were assessed regular rates. Of those mailers, at least 13 organizations were certain that they filed a corrected USPS Form 3602-R.

¹⁴ *Id.* at 35. This situation occurred in Docket No. R94-1 for In-County Publications. Through a programming error, IOCS tallies distributed costs to *In-County* publications, while revenues and volumes from those same publications were recorded under *regular rate* publications. The result was a sharp increase in the unit cost of In-County publications. The Postal Service may also have problems of this nature with respect to the various rate categories of First-Class Mail. *Id.* at 35 n. 16.

The responses come from all major geographic areas of the United States, which indicates that the phenomenon of using nonprofit evidencing on Standard Mail (A) is indeed widespread. ANM-T-1 (Haldi) at 41.

ANM is unable to offer a precise correction for this error, for the Postal Service has refused to produce data quantifying the full extent of the problem. The record does provide two reasonable methods of estimating its magnitude, however.

First, one may reasonably estimate the share of Standard (A) mail volume which paid commercial rates but bore nonprofit evidencing of postage. These data support a reduction of 7.85 percent in the mail processing costs (including piggybacks) attributed to Standard (A) nonprofit mail. *Id.* at 41-43.

In the alternative, the Commission may limit the Postal Service's proposed increase in unit attributable mail processing costs for nonprofit Standard (A) mail to the ratio of nonprofit and commercial unit attributable mail processing costs that has prevailed in recent years before FY 1996. From FY 1992 to FY 1995, the unit attributable Clerks and Mailhandlers cost for Bulk Rate Nonprofit Other mail (now called Standard (A) Nonprofit) was approximately equal to 70 percent of the unit cost for Bulk Rate Regular Other (now called Standard (A) Regular). This changed between FY 1995 and FY 1996. Specifically, the unit cost for Standard (A) Nonprofit increased by more than eight percent while the unit cost for Standard (A) Regular dropped about two percent. As the following table shows, this resulted in a ratio of the Standard (A) Nonprofit unit cost to the Standard (A) Regular unit cost of nearly 0.79:

Unit Attributable Clerks and Mailhandlers Cost (in dollars)¹⁵

Subclass	1992	1993	1994	1995	1996
Standard A Regular	0.0648	0.0664	0.0621	0.0617	0.0604
Standard A Nonprofit	0.0456	0.0457	0.0436	0.0439	0.0476
Ratio	0.7037	0.6883	0.7021	0.7115	0.7881

Limiting the Base Year Clerks and Mailhandlers costs for Standard (A) Nonprofit mail to 0.7115 times the unit cost for Standard (A) Regular mail (the ratio in FY 1995 and the highest of the ratios between FY 1992 and FY 1995) would yield a Base Year unit Clerks and Mailhandlers cost for Standard (A) Nonprofit mail of 3.8 cents, 8.6 percent less than that proposed by the Postal Service.

If the Commission declines to adopt either solution, however, the only alternative remedy would be to reject the entire increase in IOCS-related costs attributed by the Postal Service to Standard (A) nonprofit mail. Simply accepting the cost levels attributed by the Postal Service is not a lawful option. As the proponent of increases in nonprofit postal rates, the Service bears the burden of proving that the proposed increases are justified. 39 U.S.C. § 3624(a) (incorporating 5 U.S.C. § 556(d)). For nonprofit mail, the key element to be proven is the level of costs attributable to each subclass. 39 U.S.C. §§ 3622(b)(3), 3626(a)(3). The Service can hardly meet this burden with attributable cost data that are corrupted with tallies from other subclasses, particularly without offering any data setting an upward bound on the magnitude of the overstatement.

¹⁵ Source: Dividing the costs for Clerks and Mailhandlers in ANM-T-1, Table 8 by the volumes shown at the bottom of the table results in the FY 1995 and FY 1996 unit costs for Standard (A) nonprofit mail. It is a straightforward exercise to calculate unit costs for Standard (A) Nonprofit for earlier years and Standard (A) Regular for all years. For these calculations, we divided total costs from FY 1992-1996 Cost Segments and Components reports by volumes from FY 1992-1996 Cost and Revenue Analysis reports.

The Interstate Commerce Commission faced a similar issue two decades ago. Rail Form A, the cost system used in railroad rate cases at the time, attributed the variable costs of system-wide investment in railroad track, ties, and related items to individual freight movements in proportion to various measures of volume. *See San Antonio, Texas v. United States*, 631 F.2d 831, 841-42 (D.C. Cir. 1980). In the late 1970s, the ICC determined that this methodology understated the costs of new high-volume unit train coal movements for electric utilities—traffic that required massive new investments to rehabilitate the track over the route of the movement. Accordingly, the ICC allowed the railroads to attribute to individual coal movements a “fixed plant investment additive” based on the carrying costs of the capital improvements needed to handle the movements. *Id.*

The shippers argued that this additive would overstate costs unless the corresponding investment accounts were backed out of Rail Form A. *Id.* at 842. The ICC declined to back out any of the Rail Form A accounts. It conceded that including them would result in a slight, though unquantifiable overstatement of investment costs. *San Antonio, Texas v. Burlington Northern Inc.* (“*San Antonio II*”), 359 I.C.C. 1, 11-12 (1978), *aff’d*, 361 I.C.C. 482, 486-88 (1979) (“*San Antonio III*”). The ICC reasoned, however, that this consideration was insufficient to order an adjustment that would clearly understate the costs attributable to the movement by a significant amount. *Id.*

On appeal, the D.C. Circuit overturned the ICC’s action, reasoning that failure to eliminate the double-count resulted in impermissible cross-subsidization. *San Antonio*, 631 F.2d at 844. The Court’s reasoning applies with equal force here:

Variable costs by definition are only the costs caused by the relevant service and should not include costs caused by other services. We recognize that costing is not a particularly exact science, but by occasioning cross-subsidization in variable cost calculation, the

Commission's decision is not merely imprecise, but arbitrary and unreasonable.

Id.; accord, *Celanese Chemical Co. v. United States*, 632 F.2d 568, 575-76 (5th Cir. 1980). See also *Cleveland-Cliffs Iron Co. v. ICC*, 664 F.2d 568, 580-82 (6th Cir. 1981) (upholding ICC's subsequent policy of backing out Rail Form A accounts).

E. The TRACS Methodology Over-attributes Transportation Costs to Standard (A) Nonprofit Mail.

Between FY95 and FY96, the *increase* in purchased transportation costs attributed to Nonprofit Standard Mail (A) Regular amounted to \$11,451,000, an increase of 29 percent over FY95. ANM-T-1 (Haldi) at 45. Total volume of Nonprofit Standard Mail (A) Regular was up only 0.8 percent, the percentage drop shipped increased by 2 percent, and the volume variability of total transportation costs did not change between FY95 and FY96. *Id.*

This disproportionate increase in transportation costs attributed to Nonprofit Standard Mail (A) Regular stems from a fundamental design flaw of TRACS, the Postal Service's system for distributing transportation costs to individual classes and subclasses of mail. *Id.* at 45-55.

The TRACS distribution key represents the proportion of cubic foot miles that TRACS allocates to each subclass of mail. The cubic foot miles from TRACS are thus the basis for developing transportation costs attributable to each subclass. *Id.* at 45.

TRACS is a sampling system. Postage evidencing on mail pieces may be used to determine the subclass of mail. Consequently, TRACS suffers the same drawback as IOCS when nonprofit evidencing is used on mail entered at commercial rates. That is, whenever such mail is sampled, the nonprofit subclass will be tagged with the

transportation costs, while the regular rate subclass is credited with the volume and revenues. *Id.* at 46.

The purpose of TRACS is to develop a key for distributing volume variable transportation costs to the individual classes and subclasses of mail. TRACS is a sampling system, and it samples mail from postal transportation by air, highway and rail. For highway transportation, the predominant mode of transportation for nonprofit Standard (A) mail, TRACS samples mail as it is off-loaded from randomly selected trucks. *Id.* at 46.

At first blush, one might think that TRACS would distribute highway transportation costs according to:

- the *actual amount of mail* off-loaded; and
- the transportation service provided to whatever mail is found to have been off-loaded from the truck.

Id. at 46-47. Unfortunately, TRACS achieve neither of these results. TRACS treatment of highway transportation costs is fatally flawed in at least two important respects.

First, TRACS artificially breaks each truck's route into separate "independent" segments. Most highway routes involve round-trips, whereby trucks return to the facility from which they initially start the route.¹⁶ On any given day, all segments of the route are necessarily served by the same truck. Capacity of the truck must obviously be sized for whatever segment or segments have the highest average volume. In other words, the route is an integral, indivisible unit from both an

¹⁶ The truck may shuttle and back, more or less traversing the same route in each direction, or it may make a "circular" trip that does not entail retracing any segment in opposite directions. *Id.* at 47 n. 22.

operational and economic perspective. *Id.* at 47-48. As stated by Postal Service witness Bradley,

For the Postal transportation network, I view *the cost of a contract being jointly determined by the cost of serving all of the legs on all of the route/trips* on the contract. The cubic foot-mile capacity set on a contract reflects the *joint requirements* of moving mail over the Postal network and that *the total contract cost should not be allocated to any individual leg on the contract*. In other words, the cost of transportation on a contract varies with changes in the *total* cubic foot-miles specified in the contract and *is not directly allocable to any specific leg*. Moreover, contract specifications are set by the Postal Service in its attempt to minimize highway transportation costs subject to reliably meeting service standards.

7 Tr. 3337 (Bradley) (emphasis added); *accord*, ANM-T-1 (Haldi) at 47-48. In other words, the route should not be broken up artificially into “independent” segments. Yet this is precisely what TRACS does. ANM-T-1 (Haldi) at 48.

Second, TRACS is built upon an indefensible “expansion” process that distorts and biases the final distribution key by an unknown magnitude. TRACS neither measures nor records the actual volume of mail (in pieces, pounds or cube) that is off-loaded. Instead, a series of data manipulations allocates the total space available to whatever mail that happens to be off-loaded from the truck at the time when the truck is sampled. In so doing, TRACS *expands* the sampled mail *to fill the entire space available*, regardless of the amount of mail actually on the truck. ANM-T-1 (Haldi) at 48-53.

To illustrate, assume that an over-the-road (“OTR”) container is sampled upon off-loading. It may have in it only one or two sacks of nonprofit mail. Alternatively, it might be loaded full to the brim with nonprofit mail. So long as the OTR container has only nonprofit mail, it would be recorded as having 100 percent nonprofit mail. 7 Tr. 3493, 3495 (USPS witness Bradley). This is the case even if the container is practically empty and the remainder could just as easily have been filled

with something else, such as regular rate bulk mail, or parcels, or whatever. In other words, the nonprofit mail in the OTR container is treated by TRACS as somehow having been responsible for whatever empty space happens to be found in the OTR at the time the sample is taken. On this basis, TRACS treats the empty space in the container as “reasonably assignable” to the nonprofit mail in the container. ANM-T-1 (Haldi) at 48-49. Finally, because the actual volume of mail is not recorded, that most essential datum is simply unavailable in the TRACS database.¹⁷

To continue the preceding example, the TRACS expansion process does not end with the OTR container. The expansion process continues its “blame the victim” procedure until all available cube on the truck is assigned to whatever mail happens to be off-loaded from the truck, no matter how small or large the actual volume of mail. At the point where the sample is taken, the truck may be almost empty, but the expansion process nevertheless attributes all the empty space for that particular segment (as well as prior segments) to whatever mail is actually sampled.¹⁸

TRACS’ expansion process can produce bizarre results. The ratio of (1) the cubic volume attributed to a subclass and (2) the actual volume of mail on the truck can vary enormously. If the truck is practically full, the ratio will be low, perhaps less than 2 to 1. If the truck is nearly empty, however, the ratio could be quite large, perhaps exceeding 100 to 1, by virtue of the empty volume assigned to mail on the

¹⁷ *Id.* at 49. The lack of this datum makes it impossible to use the TRACS data base to develop an alternate distribution key based on actual volumes of sampled mail, and transportation services provided to sampled mail. *Id.* at 49 n. 26.

¹⁸ *Id.* at 49-50. Assume a truck is 20 percent full and three-fourths of the mail on the truck is off-loaded. Then three-fourths of the 80 percent empty capacity is “reasonably assigned” to the off-loaded mail. In this example, mail occupying 15 percent of the truck is assigned 75 percent of the total capacity of the truck for that segment. *Id.* at 50 n. 27.

truck.¹⁹ In other words, the emptier the vehicle, the greater the cube apportioned to the actual volume of mail that happens to be off-loaded from the truck. ANM-T-1 (Haldi).

On those segments that have low capacity utilization on a regular recurring basis, the cubic volume assigned to the distribution key will be inversely proportional to the actual volume of mail off-loaded from the truck. In other words, the ultimate cost that is attributed (via the distribution key) for each unit of actual mail volume will be high. Should a particular class of mail travel regularly over a segment where the truck is largely empty, that class will be the victim of this weird procedure for always attributing the entire cubic volume of the truck. Moreover, rates will be designed to reflect these unit costs, even though they may be inversely related to actual usage. *Id.* at 50-51.

In short, TRACS is an economist's nightmare come true. The emptier the vehicle, the greater the amount of cube (and, ultimately, the cost) charged to whatever subclasses of mail that happen to be on the truck. Because TRACS breaks the route into independent segments, TRACS thus operates like a game of "Old Maid" on segments where trucks are largely empty. Should volume diminish on a particular segment, until the only remaining mail on the truck is one sack or container, it gets "stuck" with the entire cube (and cost) of that particular segment (which is expanded up to the full year). It seems ironic that such an allocation procedure would be implemented by an organization which favors cost-based rates coupled with demand pricing.²⁰

¹⁹ ANM-T-1 (Haldi) at 50; 7 Tr. 3504 (USPS witness Bradley). TRACS evidence ratios of expanded cubic feet to actual feet that are well in excess of 100 to 1. 7 Tr. 3323, 3325 (Bradley).

²⁰ ANM-T-1 (Haldi) at 51-52. An analogy may help demonstrate the way TRACS assigns cubic-foot-miles that, ultimately, are reflected in "cost-based" rates.

Under TRACS, the assignment of empty space distorts the reality of what is actually being transported, and how much transportation services are actually being provided to, or consumed by, each subclass of mail. And on those occasions when trucks are largely empty, the distortion of reality can border on the grotesque. The assignment of empty space is fundamentally wrong, because no causal nexus exists between (1) the subclasses of mail on the truck and transportation services provided to that mail, and (2) empty space on the truck that is sampled.²¹

The foregoing errors systematically over attribute the costs of cubic volume to the nonprofit subclass. First, truck capacity utilization varies systematically with the direction of haul. For example, trucks bound *from* a BMC average significantly higher capacity utilization (and correspondingly less empty space) than trucks bound *to* the BMC. This variation in utilization results from the large volume of mail that is drop shipped to destination BMCs: a substantial volume of mail is transported from BMCs to destination SCFs, while originating volume traveling from SCFs to BMCs is comparatively light. ANM-T-1 (Haldi) at 53.

Suppose a ski resort spent \$10 million on a lift that is being depreciated over 10 years; *i.e.*, \$1 million per year. The average ski season at this resort lasts for 100 days, and on this basis the operator determines that depreciation of the lift costs \$10,000 per day. A random sample is taken to ascertain usage of the lift. The first sample, on Tuesday, counts 100 skiers; the second sample, on Saturday, counts 1,000 skiers. Applying TRACS reasoning, people skiing on Tuesday are assigned a depreciation cost of \$100 per skier, and for Saturday it works out to \$10 per skier. Cost-based rates for each day of the week are set accordingly. If this result seems bizarre, we rationalize it by “reasonably assigning” all the empty chairs on Tuesday to those skiers who were counted and found to be utilizing the lift that day. *Id.* at 52 n. 29.

²¹ *Id.* at 52-53. The preceding criticism of the expansion process should not in any way be interpreted to mean that some alternative way of assigning empty space on specific legs of a specific trip to individual classes of mail would be better. *Id.*

Second, nonprofit mailers systematically drop ship less than commercial mailers, and thus account for more of the volume on trucks bound to BMCs. As between the two Standard Mail (A) Regular subclasses, only 25 percent of Nonprofit Standard Mail (A) Regular was drop shipped in FY96, versus 41 percent for Standard Mail (A) Regular.²²

In sum, TRACS is fatally flawed because it fails to measure the *actual volume of mail using Postal Service transportation*, and to develop distribution keys that incorporate only actual mail volumes. TRACS also fails to treat the cost of serving an entire route as an individual unit. ANM-T-1 (Haldi) at 54. Regrettably, the circumstances of this case have not permitted development of an alternative distribution key based on the volume of mail actually transported, and the transportation services that were used by each subclass of mail. *Id.*

Given the data that are available from the TRACS sample data, the Commission could develop a distribution key that does not expand the sample beyond what the data collector initially records. That is, the expansion step or steps that unjustifiably assign absolutely empty floor space on the truck should be eliminated. This would be a step in the right direction, although it would not cure the problems identified here, or rehabilitate the TRACS data as a lawful basis for recommending the Postal Service's proposed rate increases for nonprofit mail.


²² ANM-T-1 (Haldi) at 19 (Table 6) and 54. Standard Mail (A) presorted to the 3/5-Digit category is over eight times more likely to be drop shipped than Basic Mail. If TRACS were applied at the rate category level, it would contain substantial bias against Basic presort mail. *Id.* at 54 n. 30.

CONCLUSION

For the foregoing reasons, the proposed rate increases for nonprofit Standard (A) mail should be rejected. The adjustments proposed here and in Dr. Haldi's testimony would mitigate, but not cure, the fundamental shortcomings in the Postal Service's underlying cost data.

Respectfully submitted,

Joel T. Thomas
1800 K Street, N.W., Suite 810
Washington, D.C. 20006
(703) 476- 4646


David M. Levy
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, DC 20006
(202) 736-8214

Counsel for Alliance of Nonprofit Mailers

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document on all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.

David M. Levy / dh

February 10, 1998